# INDEX


| | Page |
|---|---|
| Opinion below | 1 |
| Jurisdiction | 1 |
| Question presented | 2 |
| Statutes involved | 2 |
| Statement | 3 |
| Argument | 5 |
| Conclusion | 9 |


## CITATIONS


| | |
|---|---|
| Cases: | |
| *Commissioner* v. *Estate of Church*, 335 U.S. 632 | 8 |
| *Hertzog* v. *Commissioner*, 116 F. 2d 591 | 7 |
| *Keating* v. *Mayer*, 236 F. 2d 478 | 9 |
| *Rogers, Estate of* v. *Commissioner*, 320 U.S. 410 | 7 |
| *Wilson* v. *Kraemer*, 190 F. 2d 341, certiorari denied, 342 U.S. 859 | 9 |
| Statutes: | |
| Internal Revenue Code of 1954 (26 U.S.C., 1958 ed.): | |
| Sec. 2036 | 2, 5, 6 |
| Sec. 2041 | 3, 5 |
| Miscellaneous: | |
| Treasury Regulations on Estate Tax, Sec. 20.2041-2 | 7 |




622072—61

# In the Supreme Court of the United States

OCTOBER TERM, 1961

No. 552

ESTATE OF LEO M. GARTLAND, DECEASED,
MATTHEW GARTLAND, ADMINISTRATOR, PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT*

## BRIEF FOR THE RESPONDENT IN OPPOSITION

### OPINION BELOW

The opinion of the Court of Appeals (Pet. 48–64) is reported at 293 F. 2d 575. The opinion of the Tax Court (R. 2–21) is reported at 34 T.C. 867.

### JURISDICTION

The judgment of the Court of Appeals was entered on August 4, 1961. (Pet. 48.) A petition for rehearing was denied on September 7, 1961. The petition for a writ of certiorari was filed on November 17, 1961. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

## QUESTION PRESENTED

Whether property subject to a general power of appointment was includible in the decedent's gross estate under Section 2041(a)(1) of the Internal Revenue Code of 1954 where the decedent, by an exercise of the power, had vested in himself the right to the income and, by a subsequent surrender of the power, had caused the remainders to become vested.

## STATUTES INVOLVED

Internal Revenue Code of 1954 (26 U.S.C., 1958 ed.):

> SEC. 2036. TRANSFERS WITH RETAINED LIFE ESTATE
>
> (a) *General Rule.*—The value of the gross estate shall include the value of all property (except real property situated outside of the United States) to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death—
>
> (1) the possession or enjoyment of, or the right to the income from, the property, or
>
> (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.
>
> * * * * * *

SEC. 2041. POWERS OF APPOINTMENT

(a) *In General.*—The value of the gross estate shall include the value of all property (except real property situated outside of the United States)—

(1) *Powers of appointment created on or before October 21, 1942.*—To the extent of any property with respect to which a general power of appointment created on or before October 21, 1942, is exercised by the decedent—

(A) by will, or

(B) by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under sections 2035 to 2038, inclusive;

but the failure to exercise such a power or the complete release of such a power shall not be deemed an exercise thereof.

* * * * *

STATEMENT

1. In 1929 the decedent's father created a trust the terms of which directed the trustee, during the decedent's life:

> [¶1(A)] To pay over to my son, Leo M. Gartland [the decedent], so much of the income as the trustee in his discretion shall deem advisable and to accumulate the remaining income and add it to the principal of the trust fund * * *.

Upon the decedent's death, the income was to be paid to his wife; upon the death of both the decedent and his wife, the principal was to be divided into separate trusts for each of the decedent's children (Pet. 49).

Paragraph 8 of the trust instrument provided (Pet. 50):

> 8. I hereby authorize and empower my son, Leo M. Gartland, during his life, to amend or terminate this agreement in whole or in part and to change any beneficial interest hereunder by delivering to the Trustee an instrument in writing executed by him. In the event of the termination of this trust by my said son, the Trustee shall pay over the principal of the trust fund to him or to such person or persons as he may designate in writing to the Trustee.

2. In 1931 the decedent, by letter, instructed the trustee to pay him all the income from the trust, including that transferred to the principal account. In response, the trustee paid to the decedent all of the income previously accumulated and added to principal ($547.35) and thereafter distributed all of the net income to him (Pet. 50). In 1938, the decedent executed a formal instrument expressly ratifying his prior instructions and providing that (Pet. 51):

> * * * the said Leo M. Gartland does hereby amend said trust by striking out * * * [¶1(A)] and by substituting in lieu thereof * * *:
>
> > "A. To pay over the net income thereof to my son, Leo M. Gartland, during his life."

Finally, on June 20, 1945, the decedent executed a formal document irrevocably surrendering the power of appointment given him by paragraph 8 of the trust instrument (Pet. 52).

3. The decedent died on April 1, 1955. In estate tax deficiency proceedings, the Tax Court held that the decedent had exercised the general power of appointment given him under the trust instrument so as to render the value of the trust property includible in his estate for estate tax purposes under Sections 2041 (a)(1) and 2036(a) of the Internal Revenue Code of 1954 (R. 2–21). The Court of Appeals affirmed (Pet. 48–64).

## ARGUMENT

Both courts below correctly concluded, upon the basis of the undisputed facts, that the decedent had exercised a general power of appointment in converting a mere "hope or expectancy" under the terms of the trust into a "vested right to the income" (Pet. 54–55), and that the decedent, by a later surrender of his power of appointment, had "caused the remainders to become vested at that time" (Pet. 62). The exercise of the power effectuated a substantial change in the interests of the decedent and others in the trust estate. The subsequent surrender of the power was not a tax-free release since it was not "a complete release" within the meaning of Section 2041(a) of the 1954 Code, *supra*, p. 3. The exercise of the power, in turn, by giving the decedent a vested right to the income for life, followed by the surrender, vesting the remainders in his children, effected a disposition similar in nature to an owner's transfer of property with a retained life interest under Section 2036(a). Thus, the trust property was properly includible in the decedent's estate under Section 2041(a)(1) as property with respect to which the decedent exercised a general power of appointment "by a disposition which is of

such nature that if it were a transfer of property owned by the decedent, such property would be includible" under Section 2036(a).

Petitioner's various contentions here amount to a claim that the decedent did not make a taxable exercise of his power of appointment, because he did not make any change in the interests created by the trust (Pet. 9–10). Petitioner contends that the decedent had the right to the income either under the terms of the trust or under New York law, and that he never changed the remainder interests of his wife and children. Plainly, however, as the Court of Appeals held, the decedent "did not have the right to the income until he exercised his power of appointment" (Pet. 60). Neither the trust terms nor the New York statute prohibiting accumulations of trust income, except during the minority of a beneficiary, foreclosed the necessity of a formal and express exercise of a general power of appointment in order to secure to the decedent the absolute right to the income. As the court below held (Pet. 59–60), under New York law, it appears that the accumulated income would have been paid to the persons presumptively entitled to the next eventual estate.[1] In any event, the New York

[1] In the New York cases relied upon by the petitioner (Pet. 37) in opposition to the decisions relied upon by the court below (Pet. 60), the will or trust granted the income to the beneficiary *unless* the trustee chose to accumulate: hence, in those cases, when the accumulation was held unlawful, the grant of the income to the beneficiary became unqualified. Here there is no such grant: on the contrary, the decedent was given only as much income as the trustee chose to give him and the settlor's

law is not so clear as to have assured the decedent of the income. He chose not to rely upon the law, but upon an exercise of his general power, which is enough to constitute an exercise of a power. *Hertzog* v. *Commissioner*, 116 F. 2d 591 (C.A. 2). Hence the court below rightly concluded that "even if the provision for the accumulations of income was void by virtue of the New York Statute, the decedent did and was required to exercise the general power of appointment to obtain the income from the trust property during his life" (Pet. 60).

It follows—contrary to petitioner's contentions (Pet. 24–27)—that the decedent's surrender of the power of appointment, after it had been exercised to create a new life estate, did not constitute a mere naked, tax-free release of the power. As the court below, citing Treasury Regulations,[2] stated (Pet. 61):

---

apparent intent was to provide an estate for the decedent's widow and children, leaving it to the decedent to change the trust, if he chose, by the exercise of his general power of appointment over the entire property.

[2] See Section 20.2041-2(d) of Treasury Estate Tax Regulations which provides in part:

"If at or before the time a power of appointment is relinquished, the holder of the power exercises the power in such a manner or to such an extent that the relinquishment results in the reduction, enlargement, or shift in a beneficial interest in property, the relinquishment will be considered to be an exercise and not a release of the power."

The Tax Court further observed that by vesting the income in himself, which might otherwise have been accumulated and added to principal by the trustee, the decedent substantially reduced the value of the remainders (R. 15–16). See *Estate of Rogers* v. *Commissioner*, 320 U.S. 410.

> Clearly, the release executed in 1945 by the decedent was not a complete release, as required by section 2041(a)(1)(B), of his power of appointment, because before the execution of the release, he had taken a life estate which shifted the "beneficial interest" in the trust property from the manner in which it was to be distributed by the terms of the original trust agreement.

The petitioner's final contention that the decedent did not make a disposition similar in nature to an owner's transfer with a retained interest depends entirely upon the claim that the decedent did not make any change in the remainder interests. (Pet. 38–39.) The fact is, however, as the court below held (Pet. 61–64), that the decedent's creation of a new life estate in himself through the exercise of his general power over the entire property, confirmed by his later surrender of the power, constituted a disposition decisively akin to a transfer with a retained life interest. *Commissioner* v. *Estate of Church,* 335 U.S. 632. Moreover, the former requirement that, for an exercise of a power to be taxable, the remainder interests must pass differently than they would have under the trust provisions, was eliminated from the 1954 Code. As the Court of Appeals said, "Congress * * * intended that a tax be imposed by section 2041, not upon the 'property passing,' but upon the exercise of the general power of appointment where it existed, regardless of whether property passed under the exercise of the power of appointment or whether there was a change in the disposition of the trust property at the death of the decedent" (Pet. 57). See to the

same effect, *Keating* v. *Mayer*, 236 F. 2d 478 (C.A. 3); *Wilson* v. *Kraemer*, 190 F. 2d 341 (C.A. 2), certiorari denied, 342 U.S. 859.

## CONCLUSION

The decision below is correct, and no conflict of decisions is claimed. The petition for a writ of certiorari should be denied.

Respectfully submitted.

ARCHIBALD COX,
*Solicitor General.*

LOUIS F. OBERDORFER,
*Assistant Attorney General.*

MEYER ROTHWACKS,
JOSEPH KOVNER,
*Attorneys.*

DECEMBER 1961.

U.S. GOVERNMENT PRINTING OFFICE: 1961